

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

Quarterly Report Pursuant to Section 13 or 15 (d) of the  
Securities Exchange Act of 1934

For the quarterly period ended **March 28, 2008**

Commission File Number: 001-9249

**GRACO INC.**

(Exact name of registrant as specified in its charter)

Minnesota  
(State of incorporation)

41-0285640  
(I.R.S. Employer Identification Number)

88 - 11<sup>th</sup> Avenue N.E.  
Minneapolis, Minnesota  
(Address of principal executive offices)

55413  
(Zip Code)

(612) 623-6000  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days.

Yes   X   No       

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer   X   Accelerated filer       

Non-accelerated filer        Smaller reporting company       

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes        No   X  

60,571,000 shares of the Registrant's Common Stock, \$1.00 par value were outstanding as of April 17, 2008.

# GRACO INC. AND SUBSIDIARIES

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## PART I

**GRACO INC. AND SUBSIDIARIES**  
**Item 1. CONSOLIDATED STATEMENTS OF EARNINGS**  
(Unaudited)  
(In thousands, except per share amounts)

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Net Sales	\$204,120	\$197,495
Cost of products sold	<u>92,267</u>	<u>92,633</u>
Gross Profit	111,853	104,862
Product development	7,940	8,272
Selling, marketing and distribution	33,821	29,263
General and administrative	<u>17,738</u>	<u>15,240</u>
Operating Earnings	52,354	52,087
Interest expense	1,603	258
Other expense (income), net	<u>(115)</u>	<u>(106)</u>
Earnings before Income Taxes	50,866	51,935
Income taxes	<u>15,300</u>	<u>18,200</u>
Net Earnings	<u>\$ 35,566</u>	<u>\$ 33,735</u>
Basic Net Earnings per Common Share	\$ .58	\$ .51
Diluted Net Earnings per Common Share	\$ .57	\$ .50
Cash Dividends Declared per Common Share	\$ .19	\$ .17

See notes to consolidated financial statements.

**GRACO INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**

(Unaudited)  
(In thousands)

	<u>March 28, 2008</u>	<u>Dec. 28, 2007</u>
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents	\$ 6,778	\$ 4,922
Accounts receivable, less allowances of \$7,900 and \$6,500	150,726	140,489
Inventories	88,496	74,737
Deferred income taxes	25,510	21,650
Other current assets	<u>2,741</u>	<u>7,034</u>
Total current assets	274,251	248,832
 Property, Plant and Equipment		
Cost	311,180	306,073
Accumulated depreciation	<u>(169,625)</u>	<u>(165,479)</u>
Property, plant and equipment, net	141,555	140,594
 Prepaid Pension	32,495	31,823
Goodwill	84,887	67,204
Other Intangible Assets, net	58,021	41,889
Other Assets	<u>6,538</u>	<u>6,382</u>
Total Assets	<u>\$ 597,747</u>	<u>\$ 536,724</u>
 <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current Liabilities		
Notes payable to banks	\$ 19,566	\$ 18,991
Trade accounts payable	32,393	27,379
Salaries, wages and commissions	14,085	20,470
Dividends payable	11,169	11,476
Other current liabilities	<u>57,052</u>	<u>47,561</u>
	134,265	125,877
 Long-Term Debt	178,595	107,060
Retirement Benefits and Deferred Compensation	40,944	40,639
Uncertain Tax Positions	1,650	5,400
Deferred Income Taxes	19,104	13,074
 Shareholders' Equity		
Common stock	60,692	61,964
Additional paid-in capital	166,080	156,420
Retained earnings	4,792	32,986
Accumulated other comprehensive income (loss)	<u>(8,375)</u>	<u>(6,696)</u>
Total shareholders' equity	223,189	244,674
Total Liabilities and Shareholders' Equity	<u>\$ 597,747</u>	<u>\$ 536,724</u>

See notes to consolidated financial statements.

**GRACO INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)  
(In thousands)

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
<b>Cash Flows from Operating Activities</b>		
Net Earnings	\$ 35,566	\$ 33,735
Adjustments to reconcile net earnings to net cash provided by operating activities		
Depreciation and amortization	7,395	6,959
Deferred income taxes	(2,885)	(3,478)
Share-based compensation	2,553	2,218
Excess tax benefit related to share-based payment arrangements	(1,723)	(848)
Change in		
Accounts receivable	(5,296)	(7,631)
Inventories	(9,836)	(10,985)
Trade accounts payable	4,801	1,711
Salaries, wages and commissions	(6,808)	(12,469)
Retirement benefits and deferred compensation	(887)	(989)
Other accrued liabilities	9,204	15,081
Other	(228)	(165)
<b>Net cash provided by operating activities</b>	<u>31,856</u>	<u>23,139</u>
<b>Cash Flows from Investing Activities</b>		
Property, plant and equipment additions	(5,130)	(13,267)
Proceeds from sale of property, plant and equipment	39	149
Capitalized software and other intangible asset additions	(222)	—
Acquisition of business, net of cash acquired	(35,266)	—
<b>Net cash used in investing activities</b>	<u>(40,579)</u>	<u>(13,118)</u>
<b>Cash Flows from Financing Activities</b>		
Net borrowings (payments) on short-term lines of credit	(818)	14,939
Borrowings on long-term line of credit	83,335	—
Payments on long-term line of credit	(11,800)	—
Excess tax benefit related to share-based payment arrangements	1,723	848
Common stock issued	9,811	8,355
Common stock retired	(59,528)	(23,985)
Cash dividends paid	(11,376)	(11,010)
<b>Net cash provided by (used in) financing activities</b>	<u>11,347</u>	<u>(10,853)</u>
Effect of exchange rate changes on cash	(768)	(272)
Net increase (decrease) in cash and cash equivalents	1,856	(1,104)
Cash and cash equivalents		
Beginning of year	4,922	5,871
End of period	<u>\$ 6,778</u>	<u>\$ 4,767</u>

See notes to consolidated financial statements.

**GRACO INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

1. The consolidated balance sheet of Graco Inc. and Subsidiaries (the Company) as of March 28, 2008 and the related statements of earnings and cash flows for the thirteen weeks then ended have been prepared by the Company and have not been audited.

In the opinion of management, these consolidated statements reflect all adjustments (consisting of only normal recurring adjustments) necessary to present fairly the financial position of Graco Inc. and Subsidiaries as of March 28, 2008, and the results of operations and cash flows for all periods presented.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. Therefore, these statements should be read in conjunction with the financial statements and notes thereto included in the Company's 2007 Annual Report on Form 10-K.

The results of operations for interim periods are not necessarily indicative of results that will be realized for the full fiscal year.

2. The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share amounts):

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Net earnings available to common shareholders	\$35,566	\$33,735
Weighted average shares outstanding for basic earnings per share	61,254	66,667
Dilutive effect of stock options computed based on the treasury stock method using the average market price	663	1,048
Weighted average shares outstanding for diluted earnings per share	61,917	67,715
Basic earnings per share	\$ .58	\$ .51
Diluted earnings per share	\$ .57	\$ .50

Stock options to purchase 2,215,000 and 948,000 shares were not included in the 2008 and 2007 calculations of diluted earnings per share, respectively, because they would have been anti-dilutive.

3. Information on option shares outstanding and option activity for the thirteen weeks ended March 28, 2008 is shown below (in thousands, except per share amounts):

	<u>Option Shares</u>	<u>Weighted Average Exercise Price</u>	<u>Options Exercisable</u>	<u>Weighted Average Exercise Price</u>
Outstanding, December 28, 2007	3,779	\$28.63	2,228	\$21.41
Granted	676	35.87		
Exercised	(210)	15.90		
Canceled	<u>(160)</u>	38.95		
Outstanding, March 28, 2008	<u>4,085</u>	\$30.08	2,353	\$24.02

The aggregate intrinsic value of exercisable option shares was \$30.7 million as of March 28, 2008, with a weighted average contractual term of 4.8 years. There were approximately 4 million vested share options and share options expected to vest as of March 28, 2008, with an aggregate intrinsic value of \$31.1 million, a weighted average exercise price of \$29.94 and a weighted average contractual term of 6.6 years.

Information related to options exercised in the first three months of 2008 and 2007 follows (in thousands):

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Cash received	\$3,329	\$1,305
Aggregate intrinsic value	4,134	3,407
Tax benefit realized	1,500	1,200

The Company recognized share-based compensation of \$2.6 million in the first quarter of 2008 and \$2.2 million in the first quarter of 2007. As of March 28, 2008, there was \$12.5 million of unrecognized compensation cost related to unvested options, expected to be recognized over a weighted average period of 2.7 years.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions and results:

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Expected life in years	6.0	6.0
Interest rate	3.1%	4.6%
Volatility	25.0%	26.2%
Dividend yield	2.1%	1.6%
Weighted average fair value per share	\$8.32	\$12.05

Under the Company's Employee Stock Purchase Plan, the Company issued 216,000 shares in 2008 and 202,000 shares in 2007. The fair value of the employees' purchase rights under this Plan was estimated on the date of grant. The benefit of the 15 percent discount from the lesser of the fair market value per common share on the first day and the last day of the plan year was added to the fair value of the employees' purchase rights determined using the Black-Scholes option-pricing model with the following assumptions and results:

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Expected life in years	1.0	1.0
Interest rate	1.5%	4.9%
Volatility	27.1%	24.4%
Dividend yield	2.1%	1.6%
Weighted average fair value per share	\$8.14	\$9.79

4. The components of net periodic benefit cost for retirement benefit plans were as follows (in thousands):

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
<b>Pension Benefits</b>		
Service cost	\$ 1,391	\$ 1,479
Interest cost	3,146	2,882
Expected return on assets	(4,850)	(4,800)
Amortization and other	152	255
Net periodic benefit cost (credit)	<u>\$ (161)</u>	<u>\$ (184)</u>
<b>Postretirement Medical</b>		
Service cost	\$ 125	\$ 150
Interest cost	375	300
Amortization and other	—	(50)
Net periodic benefit cost	<u>\$ 500</u>	<u>\$ 400</u>

5. Total comprehensive income was as follows (in thousands):

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Net earnings	\$35,566	\$33,735
Pension and postretirement medical liability adjustment	124	(14)
Gain (loss) on interest rate hedge contracts	(2,775)	—
Cumulative translation adjustment	(5)	(7)
Income taxes	977	5
Comprehensive income	<u>\$33,887</u>	<u>\$33,719</u>

Components of accumulated other comprehensive income (loss) were (in thousands):

	<u>March 28, 2008</u>	<u>Dec. 28, 2007</u>
Pension and postretirement medical liability adjustment	\$(5,597)	\$(5,672)
Gain (loss) on interest rate hedge contracts	(2,821)	(1,072)
Cumulative translation adjustment	<u>43</u>	<u>48</u>
Total	<u>\$(8,375)</u>	<u>\$(6,696)</u>

6. The Company has three reportable segments: Industrial, Contractor and Lubrication. The Company does not track assets by segment. Sales and operating earnings by segment for the thirteen weeks ended March 28, 2008 and March 30, 2007 were as follows (in thousands):

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
<b>Net Sales</b>		
Industrial	\$ 114,251	\$ 105,065
Contractor	66,180	69,751
Lubrication	<u>23,689</u>	<u>22,679</u>
Consolidated	<u>\$ 204,120</u>	<u>\$ 197,495</u>
<b>Operating Earnings</b>		
Industrial	\$ 37,898	\$ 34,418
Contractor	13,696	17,027
Lubrication	4,317	3,064
Unallocated corporate	<u>(3,557)</u>	<u>(2,422)</u>
Consolidated	<u>\$ 52,354</u>	<u>\$ 52,087</u>

7. Major components of inventories were as follows (in thousands):

	<u>March 28, 2008</u>	<u>Dec. 28, 2007</u>
Finished products and components	\$ 55,402	\$ 46,677
Products and components in various stages of completion	26,262	24,805
Raw materials and purchased components	<u>40,231</u>	<u>37,311</u>
	121,895	108,793
Reduction to LIFO cost	<u>(33,399)</u>	<u>(34,056)</u>
Total	<u>\$ 88,496</u>	<u>\$ 74,737</u>

8. Information related to other intangible assets follows (dollars in thousands):

	<u>Estimated Life (Years)</u>	<u>Original Cost</u>	<u>Amorti- zation</u>	<u>Foreign Currency Translation and Other</u>	<u>Book Value</u>
<u>March 28, 2008</u>					
Customer relationships	3 – 8	\$37,230	\$ (9,021)	\$ 28	\$28,237
Patents, proprietary technology and product documentation	3 – 15	23,598	(8,566)	14	15,046
Trademarks and trade names	3 – 10	<u>4,684</u>	<u>(2,878)</u>	<u>22</u>	<u>1,828</u>
		65,512	(20,465)	64	45,111
Not Subject to Amortization: Brand names		<u>12,910</u>	<u>—</u>	<u>—</u>	<u>12,910</u>
Total		<u>\$78,422</u>	<u>\$(20,465)</u>	<u>\$ 64</u>	<u>\$58,021</u>
<u>December 28, 2007</u>					
Customer relationships and distribution network	4 – 8	\$26,102	\$(11,092)	\$ 29	\$15,039
Patents, proprietary technology and product documentation	5 – 15	22,243	(7,720)	16	14,539
Trademarks, trade names and other	3 – 10	<u>4,684</u>	<u>(2,555)</u>	<u>22</u>	<u>2,151</u>
		53,029	(21,367)	67	31,729
Not Subject to Amortization: Brand names		<u>10,160</u>	<u>—</u>	<u>—</u>	<u>10,160</u>
Total		<u>\$63,189</u>	<u>\$(21,367)</u>	<u>\$ 67</u>	<u>\$41,889</u>

Amortization of intangibles was \$2.3 million in the first quarter of 2008. Estimated annual amortization expense is as follows: \$10.2 million in 2008, \$9.5 million in 2009, \$8.5 million in 2010, \$7.5 million in 2011, \$6.8 million in 2012 and \$4.9 million thereafter.

9. Components of other current liabilities were (in thousands):

	<u>March 28, 2008</u>	<u>Dec. 28, 2007</u>
Accrued self-insurance retentions	\$ 7,909	\$ 7,842
Accrued warranty and service liabilities	7,423	7,084
Accrued trade promotions	3,787	6,480
Payable for employee stock purchases	825	5,829
Income taxes payable	12,807	678
Other	<u>24,301</u>	<u>19,648</u>
	<u>\$ 57,052</u>	<u>\$ 47,561</u>

A liability is established for estimated future warranty and service claims that relate to current and prior period sales. The Company estimates warranty costs based on historical claim experience and other factors including evaluating specific product warranty issues. Following is a summary of activity in accrued warranty and service liabilities (in thousands):

	Thirteen Weeks Ended March 28, 2008	Year Ended Dec. 28, 2007
Balance, beginning of year	\$ 7,084	\$ 6,675
Charged to expense	1,421	6,053
Margin on parts sales reversed	1,253	3,186
Reductions for claims settled	<u>(2,335)</u>	<u>(8,830)</u>
Balance, end of period	<u>\$ 7,423</u>	<u>\$ 7,084</u>

10. The examination of the Company's U.S. income tax returns for 2004 and 2005 was completed in the first quarter of 2008. Completion of the examination resulted in a payment of approximately \$1 million and reductions of uncertain tax positions totaling approximately \$4 million. The settlement of the examination decreased the Company's effective tax rate for the quarter to 30 percent.

With few exceptions, the Company is no longer subject to U.S. federal, state and local, or foreign income tax examinations by tax authorities for years prior to 2002.

11. In February 2008, the Company acquired GlasCraft Inc. for approximately \$35 million cash. GlasCraft has an office and manufacturing facility in Indianapolis, Indiana and had sales of approximately \$18 million in 2007. It designs, manufactures and sells spray systems for the composites manufacturing industry and high performance dispense systems for the polyurethane foam and polyurea coatings industries. The products, brands, distribution channels and engineering capabilities of GlasCraft will expand and complement the Company's Industrial Equipment business.

The purchase price has not been finalized and is subject to final determination of acquired asset and liability balances. The preliminary purchase price was allocated based on estimated fair values as follows (in thousands):

Accounts receivable and prepaid expenses	\$ 2,200
Inventories	3,700
Deferred income taxes	700
Property, plant and equipment	700
Identifiable intangible assets	18,200
Goodwill	<u>17,700</u>
Total purchase price	43,200
Current liabilities assumed	(1,000)
Deferred income taxes	<u>(6,900)</u>
Net assets acquired	<u>\$35,300</u>

Identifiable intangible assets and weighted average estimated useful life are as follows (dollars in thousands):

Product documentation (5 years)	\$ 900
Customer relationships (6 years)	14,100
Proprietary technology (3 years)	<u>500</u>
Total (6 years)	15,500
Brand name (indefinite useful life)	<u>2,700</u>
Total identifiable intangible assets	<u><u>\$18,200</u></u>

None of the goodwill or identifiable intangible assets is expected to be deductible for tax purposes.

12. In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 157, "Fair Value Measurements." This statement establishes a consistent framework for measuring fair value and expands disclosures on fair value measurements. SFAS No. 157 was effective for the Company starting in fiscal 2008 with respect to financial assets and liabilities. The impact of the initial adoption of SFAS No. 157 in 2008 had no impact on the consolidated financial statements.

The Company uses significant other observable inputs to value the derivative instruments used to hedge interest rate volatility and net monetary positions. The fair market value of such instruments follows (in thousands):

	<u>March 28, 2008</u>	<u>Dec. 28, 2007</u>
Gain (loss) on interest rate hedge contracts	\$(4,475)	\$(1,700)
Gain (loss) on foreign currency forward contracts	<u>(401)</u>	<u>(282)</u>
Total	<u><u>\$(4,876)</u></u>	<u><u>\$(1,982)</u></u>

With respect to non-financial assets and liabilities, SFAS No. 157 is effective for the Company starting in fiscal 2009. The Company has not determined the impact, if any, the adoption of this statement as it pertains to non-financial assets and liabilities will have on its consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities." This statement expands disclosures but does not change accounting for derivative instruments and hedging activities. The statement is effective for the Company starting in fiscal 2009.

**Item 2.****GRACO INC. AND SUBSIDIARIES**

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**Results of Operations**

Net sales, net earnings and earnings per share were as follows (in thousands except per share amounts and percentages):

	<u>Thirteen Weeks Ended</u>		<u>% Change</u>
	<u>March 28, 2008</u>	<u>March 30, 2007</u>	
Net Sales	\$204,120	\$197,495	3%
Net Earnings	35,566	33,735	5%
Diluted Net Earnings per Common Share	\$ 0.57	\$ 0.50	14%

Foreign currency translation rates had a favorable impact on first quarter sales and net earnings. Translated at consistent exchange rates, sales were flat compared to 2007 and net earnings decreased 4 percent.

Results include sales of \$1.5 million from GlasCraft, which was acquired in late February 2008.

Earnings per share increased at a higher rate than net earnings due to purchases and retirement of approximately 1.7 million shares of Company common stock.

**Consolidated Results**

Sales by geographic area were as follows (in thousands):

	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Americas <sup>1</sup>	\$ 115,833	\$ 120,546
Europe <sup>2</sup>	59,508	49,377
Asia Pacific	28,779	27,572
Consolidated	<u>\$ 204,120</u>	<u>\$ 197,495</u>

<sup>1</sup> North and South America, including the U.S.

<sup>2</sup> Europe, Africa and Middle East

The decrease in the Americas, driven by weakness in the Contractor business, was more than offset by the increase in Europe, where net sales were 21 percent higher than last year. Translated at consistent exchange rates, net sales in Europe increased 9 percent. In the Asia Pacific region, net sales were 4 percent higher than last year, with half of the increase from favorable currency translation.

Gross profit margin, expressed as a percentage of sales, was 54.8 percent versus 53.1 percent for the same period last year. The increase was due mainly to favorable currency translation rates. The benefits of integrating Lubriquip and consolidating the Lubrication

Equipment operations in the Company's Anoka facility are also beginning to be reflected in the gross profit margin percentage.

Operating profit margin, expressed as a percentage of sales, was 25.6 percent for the first quarter versus 26.4 percent last year. Operating expenses in 2008 include approximately \$1 million related to the rollout of the new sprayer line in the home center channel, approximately \$1 million from GlasCraft operations and a \$1 million contribution to the Company's charitable foundation. The effects of currency translation increased operating expenses by approximately \$2 million.

The \$1.3 million increase in interest expense resulted from borrowings used to purchase and retire Company shares and for the acquisition of GlasCraft.

The Company's effective tax rate for the first quarter was 30 percent, down from 35 percent for the first quarter last year. The decrease resulted from the completion of the examination of the Company's income tax returns.

## Segment Results

Certain measurements of segment operations compared to the first quarter of last year are summarized below:

### Industrial

Net sales (in thousands)	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Americas	\$ 53,403	\$ 50,475
Europe	39,650	32,447
Asia Pacific	<u>21,198</u>	<u>22,143</u>
Total	<u>\$114,251</u>	<u>\$105,065</u>
Operating earnings as a percentage of net sales	<u>33%</u>	<u>33%</u>

Net sales in the Industrial segment were up 6 percent in the Americas and 22 percent in Europe. Approximately half of the percentage increase in Europe came from currency translation.

### Contractor

Net sales (in thousands)	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Americas	\$42,362	\$50,580
Europe	17,962	15,134
Asia Pacific	<u>5,856</u>	<u>4,037</u>
Total	<u>\$66,180</u>	<u>\$69,751</u>
Operating earnings as a percentage of net sales	<u>21%</u>	<u>24%</u>

In the Contractor segment, net sales increases in Europe and Asia Pacific were not enough to offset a 16 percent decrease in the Americas, where sales were down in both the paint store and home center channels. Operating earnings in this segment were affected by \$2.5 million related to the launch and production of new paint sprayer units in the home center channel.

## Lubrication

Net sales (in thousands)	<u>Thirteen Weeks Ended</u>	
	<u>March 28, 2008</u>	<u>March 30, 2007</u>
Americas	\$20,068	\$19,491
Europe	1,896	1,796
Asia Pacific	1,725	1,392
Total	<u>\$23,689</u>	<u>\$22,679</u>
Operating earnings as a percentage of net sales	<u>18%</u>	<u>14%</u>

Most sales, and sales growth, in the Lubrication segment came from the Americas. The improvement in operating profitability is related to the integration and consolidation of Lubrication operations completed in 2007.

## **Liquidity and Capital Resources**

The Company used cash and borrowings under its long-term line of credit to purchase and retire \$60 million of Company shares. Other significant uses of cash in the first quarter of 2008 included \$35 million to acquire GlasCraft and \$11 million for payment of dividends. Significant uses of cash in the first quarter of 2007 included \$24 million for purchases and retirement of Company common stock, \$13 million for capital additions and \$11 million for payment of dividends.

At March 28, 2008, the Company had various lines of credit totaling \$295 million, of which \$101 million was unused. Internally generated funds and unused financing sources provide the Company with the financial flexibility to meet liquidity needs.

## **Outlook**

Management is encouraged by the gains in the Company's Industrial and Lubrication segments in North America and by the continued strength of its international business, including the Asia Pacific region, where orders were 15 percent higher than last year. Based on continuing weakness in the U.S. housing market, management remains cautious about the outlook for the Contractor business in North America and will manage the business accordingly. The Company will continue to make long-term investments in key growth strategies including new product development, expanding distribution, entering new markets and pursuing strategic acquisitions.

## **SAFE HARBOR CAUTIONARY STATEMENT**

A forward-looking statement is any statement made in this report and other reports that the Company files periodically with the Securities and Exchange Commission, or in press or earnings releases, analyst briefings and conference calls, which reflects the Company's current thinking on market trends and the Company's future financial performance at the time they are made. All forecasts and projections are forward-looking statements.

The Company desires to take advantage of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995 by making cautionary statements concerning any forward-looking statements made by or on behalf of the Company. The Company cannot give any assurance that the results forecasted in any forward-looking statement will actually be achieved. Future results could differ materially from those expressed, due to the impact of changes in various factors. These risk factors include, but are not limited to: economic conditions in the United States and other major world economies, currency fluctuations, political instability, changes in laws and regulations, and changes in product demand. Please refer to Item 1A of, and Exhibit 99 to, the Company's Annual Report on Form 10-K for fiscal year 2007 for a more comprehensive discussion of these and other risk factors.

Investors should realize that factors other than those identified above and in Item 1A and Exhibit 99 might prove important to the Company's future results. It is not possible for management to identify each and every factor that may have an impact on the Company's operations in the future as new factors can develop from time to time.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

There have been no material changes related to market risk from the disclosures made in the Company's 2007 Annual Report on Form 10-K.

### **Item 4. Controls and Procedures**

#### **Evaluation of disclosure controls and procedures**

As of the end of the fiscal quarter covered by this report, the Company carried out an evaluation of the effectiveness of the design and operation of its disclosure controls and procedures. This evaluation was done under the supervision and with the participation of the Company's President and Chief Executive Officer, the Chief Financial Officer and Treasurer, the Vice President and Controller, and the Vice President, General Counsel and Secretary. Based upon that evaluation, they concluded that the Company's disclosure controls and procedures are effective in gathering, analyzing and disclosing information needed to satisfy the Company's disclosure obligations under the Exchange Act.

#### **Changes in internal controls**

During the quarter, there was no change in the Company's internal control over financial reporting that has materially affected or is reasonably likely to materially affect the Company's internal control over financial reporting.

## PART II OTHER INFORMATION

### Item 1A. Risk Factors

There have been no material changes to the Company's risk factors from those disclosed in the Company's 2007 Annual Report on Form 10-K.

### Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

#### Issuer Purchases of Equity Securities

On September 28, 2007, the Board of Directors authorized the Company to purchase up to a total of 7,000,000 shares of its outstanding common stock, primarily through open-market transactions. This authorization expires on September 30, 2009.

In addition to shares purchased under the Board authorizations, the Company purchases shares of common stock held by employees who wish to tender owned shares to satisfy the exercise price or tax withholding on option exercises.

Information on issuer purchases of equity securities follows:

<u>Period</u>	<u>(a) Total Number of Shares Purchased</u>	<u>(b) Average Price Paid per Share</u>	<u>(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</u>	<u>(d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs (at end of period)</u>
Dec 29, 2007 – Jan 25, 2008	709,319	\$34.40	709,319	5,438,214
Jan 26, 2008 – Feb 22, 2008	169,032	\$34.08	159,000	5,279,214
Feb 23, 2008 – Mar 28, 2008	821,501	\$35.03	819,259	4,459,955

### Item 4. Submission of Matters to a Vote of Security Holders

None

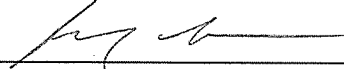
**Item 6. Exhibits**

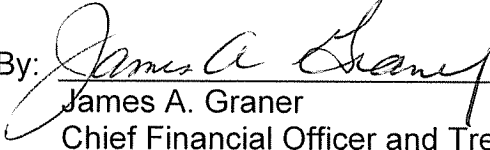
- 10.1 Graco Restoration Plan (2005 Statement). Third Amendment adopted March 27, 2008.
- 10.2 Stock Option Agreement. Form of agreement used for award in 2008 of non-incentive stock options to executive officers under the Graco Inc. Amended and Restated Stock Incentive Plan (2006). Form of agreement for award made to Chief Executive Officer in 2008.
- 31.1 Certification of President and Chief Executive Officer pursuant to Rule 13a-14(a).
- 31.2 Certification of Chief Financial Officer and Treasurer pursuant to Rule 13a-14(a).
- 32 Certification of the President and Chief Executive Officer and the Chief Financial Officer and Treasurer pursuant to Section 1350 of Title 18, U.S.C.

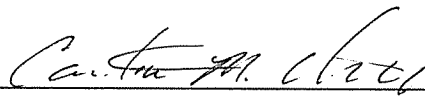
## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

### GRACO INC.

Date: 4-23-08 By:   
Patrick J. McHale  
President and Chief Executive Officer  
(Principal Executive Officer)

Date: April 23, 2008 By:   
James A. Graner  
Chief Financial Officer and Treasurer  
(Principal Financial Officer)

Date: April 23, 2008 By:   
Caroline M. Chambers  
Vice President and Controller  
(Principal Accounting Officer)

**GRACO INC.**

**GRACO RESTORATION PLAN  
(2005 STATEMENT)**

**THIRD AMENDMENT**

**Written Action  
Of  
Chief Executive Officer**

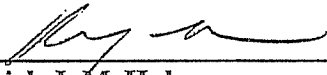
**WHEREAS**, Graco Inc. ("Graco"), a Minnesota corporation, has adopted the Graco Restoration Plan (2005 Statement) (the "Plan Statement");

**WHEREAS**, Section 9.1 of the Plan Statement provides that Graco may amend the Plan Statement in any respect by action of its Board of Directors; and

**WHEREAS**, the Board of Directors of Graco, by resolution adopted at its meeting held on June 14, 2007, delegated to the Chief Executive Officer the authority to amend the Plan Statement to allow distribution forms under the Plan Statement similar to those available under the Graco Employee Retirement Plan (1991 Restatement) and to permit a lump sum distribution form while retaining the existing default distribution forms.

**NOW, THEREFORE, BE IT RESOLVED**, based on the authority delegated to me, I adopt the attached Third Amendment to the Plan Statement.

3-21-08  
Date

  
\_\_\_\_\_  
Patrick J. McHale  
Chief Executive Officer  
Graco Inc.

**THIRD AMENDMENT  
GRACO RESTORATION PLAN  
(2005 Statement)**

Graco Inc. (the "Principal Sponsor") has established and maintains a nonqualified deferred compensation plan (the "Plan") which, in its most recent amended and restated form, is embodied in a document entitled "GRACO RESTORATION PLAN (2005 Statement)" effective January 1, 2005 (as amended, the "Plan Statement") and is hereby amended as follows:

**1. DISTRIBUTION FORMS.** Effective for distributions made on and after July 1, 2007, Subsection 7.1.2 shall be amended (i) to re-number Subsection 7.1.2(b) as Subsection 7.1.2(d), and (ii) to add the following new Subsections 7.1.2(b) and 7.1.2(c) that read in full as follows:

- (b) **Election to Change the Form or Delay the Time of Distribution.** A Participant may make an election to change the form or delay the time of distribution. If (i) a Participant's form of payment prior to electing one of the alternative forms of payment listed below is an annuity, (ii) the Participant elects an alternative form that is an annuity (options (i), (ii), (iii), (iv), (v), and (vi), but not (vii) – the lump sum form), and (iii) the annuity elected is actuarially equivalent applying reasonable actuarial methods and assumptions, then the Participant's benefit shall commence on the same date the benefit would have been paid but for the election of the alternative form. In all other cases, if a Participant elects one of these alternative forms of payment, the election (i) shall not take effect until the date that is twelve (12) months after the date on which the Participant makes the election, (ii) shall delay the distribution to a date that is at least five (5) years after the date the distribution would have been made to the Participant absent the election, and (iii) in the case of a distribution as of a specified time (but not upon a Participant's Separation from Service, Disability, or death), the election shall not take effect unless the Participant makes the election at least twelve (12) months prior to the date the distribution is to commence. An election form that does not satisfy the advance filing requirements of the preceding sentence shall be void and shall be disregarded. In all cases an election form shall not be considered filed until the completed form is actually received by the Committee or its designated agent.
- (c) **Alternate Forms of Distribution.** Subject to satisfying the conditions in Section 7.1.4(b), the participant may elect to receive distribution the following forms
  - (i) A fifty percent (50%) survivor annuity.

- (ii) A sixty-six and two-thirds percent (66-2/3%) survivor annuity (available only if the joint annuitant is not more than twenty-four (24) years younger than the Participant).
- (iii) A seventy-five percent (75%) survivor annuity.
- (iv) A one hundred percent (100%) survivor annuity (available only if the joint annuitant is not more than ten (10) years younger than the Participant).
- (v) A term certain single life annuity based on the Participant's life with a term certain period of one hundred twenty (120) months (available only if the Participant has not attained age 92).
- (vi) A term certain single life annuity based on the Participant's life with a term certain period of one hundred eighty (180) months (available only if the Participant has not attained age 84).
- (vii) A single lump sum payment.

The actuarial determination of all forms in section 7.1.2 shall be based upon the terms of the Graco Employee Retirement Plan.

**2. SAVINGS CLAUSE.** Save and except as hereinabove expressly amended, the Restoration Plan shall continue in full force and effect.

**GRACO INC.  
AMENDED AND RESTATED STOCK INCENTIVE PLAN (2006)**

**EXECUTIVE OFFICER  
STOCK OPTION AGREEMENT  
(Non-Qualified)**

**THIS AGREEMENT**, made this «Day\_of\_Month\_» day of «Month\_and\_Year», by and between Graco Inc., a Minnesota corporation (the "Company") and «F\_Name\_MI» «L\_Name» (the "Employee").

**WITNESSETH THAT:**

**WHEREAS**, the Company pursuant to the Graco Inc. Amended and Restated Stock Incentive Plan (2006) (the "Plan") wishes to grant this stock option to Employee;

**NOW THEREFORE**, in consideration of the premises and of the mutual covenants contained in this Agreement, the parties agree as follows:

1. Grant of Option

The Company grants to Employee, the right and option (the "Option") to purchase all or any part of an aggregate of «Words» («Number») shares of Common Stock of the Company, par value USD 1.00 per share, at the price of USD «Price» per share on the terms and conditions set forth in this Agreement. The date of grant of the Option is «Date» (the "Date of Grant").

2. Duration and Exercisability

- A. No portion of this Option may be exercised by Employee until the first anniversary of the Date of Grant and then only in accordance with the Vesting Schedule set forth below. In no event shall this Option or any portion of this Option be exercisable following the tenth anniversary of the Date of Grant.

**Vesting Schedule**

<u>Vesting Date</u>	<u>Portion of Option Exercisable</u>
First Anniversary of Date of Grant	25%
Second Anniversary of Date of Grant	50%
Third Anniversary of Date of Grant	75%
Fourth Anniversary of Date of Grant	100%

If Employee does not purchase in any one year the full number of shares of Common Stock of the Company to which he/she is entitled under this Option, he/she may, subject to the terms and conditions of Section 3, purchase such

shares of Common Stock in any subsequent year during the term of this Option. This Option shall expire as of the close of trading at the national securities exchange on which the Common Stock is traded ("Exchange") on the tenth anniversary of the Date of Grant or if the Exchange is closed on the anniversary date or the Common Stock of the Company is not trading on said anniversary date, such earlier business day on which the Common Stock is trading on the Exchange.

- B. During the lifetime of Employee, the Option shall be exercisable only by him/her and shall not be assignable or transferable by him/her otherwise than by will or the laws of descent and distribution.
- C. Under no circumstances may the Option or any portion of the Option granted by this Agreement be exercised after the term of the Option expires.

3. Effect of Termination of Employment

- A. If Employee's employment terminates for any reason other than Employee's gross and willful misconduct, death, retirement (as defined in Section 3D), or disability (as defined in Section 3D), Employee shall have the right to exercise that portion of the Option exercisable upon the date of termination of employment at any time within the period beginning on the day after termination of employment and ending at the close of trading on the Exchange thirty (30) days later.
- B. If Employee's employment terminates by reason of Employee's gross and willful misconduct during employment, including, but not limited to, wrongful appropriation of Company funds, serious violations of Company policy, breach of fiduciary duty or the conviction of a felony, the unexercised portion of the Option shall terminate as of the time of the misconduct. If the Company determines subsequent to the termination of Employee's employment for whatever reason, that Employee engaged in conduct during employment that would constitute gross and willful misconduct justifying termination, the Option shall terminate as of the time of such misconduct. Furthermore, if the Option is exercised in whole or in part and the Company thereafter determines that Employee engaged in gross and willful misconduct during employment which would have justified termination at any time prior to the date of such exercise, the Option shall be deemed to have terminated as of the time of the misconduct and the Company may elect to rescind the Option exercise.
- C. If Employee shall die while employed by the Company or an affiliate and shall not have fully exercised the Option, all shares remaining under the Option shall become immediately exercisable. If Employee shall die within thirty (30) days after a termination of employment which meets the criteria of Section 3A above, only those shares vested as of the date of termination shall be exercisable. The executor or administrator of Employee's estate, or any person(s) to whom the Option was transferred by will or the applicable laws of distribution and descent may exercise such exercisable shares at any time during a period beginning on the day after the date of Employee's death and ending at the close of trading on the Exchange on the anniversary of death one (1) year later.

- D. If Employee's termination of employment is due to retirement or disability, all shares remaining under the Option shall become immediately exercisable. Employee shall be deemed to have retired if the termination of employment occurs for reasons other than the Employee's gross and willful misconduct, death, or disability after Employee (i) has attained age 55 and 10 years of service with the Company or an affiliate, or (ii) has attained age 65. Employee shall be deemed to be disabled if the termination of employment occurs because Employee is unable to work due to an impairment which would qualify as a disability under the Company's long term disability program. Employee may exercise the shares remaining unexercised at any time during a period beginning on the day after the date of Employee's termination of employment and ending at the close of trading on the Exchange on the tenth anniversary of the Date of Grant. If Employee should die during the period between the date of Employee's retirement or disability and the expiration of the Option, the executor(s) or administrator(s) of the Employee's estate, or any person(s) to whom the Option was transferred by will or the applicable laws of distribution and descent may exercise the unexercised portion of the Option at any time during a period beginning the day after the date of Employee's death and ending at the close of trading on the Exchange on the anniversary of death one (1) year later, provided, however, in no event shall the Option be exercisable following the tenth anniversary of the Date of Grant.
- E. Notwithstanding anything to the contrary contained in this Section 3, if the Employee's employment is terminated by retirement (as defined in Section 3D) and Employee has not given the Company written notice to his/her immediate supervisor and the Chief Executive Officer, of Employee's intention to retire not less than six (6) months prior to the date of his/her retirement, then in such event, for purposes of this Agreement only, said termination of employment shall be deemed to be not a retirement but a termination subject to the provisions of Section 3A, *provided, however*, that in the event that the Chief Executive Officer determines that said termination of employment without six (6) months prior written notice is in the best interests of the Company, such termination shall be deemed to be a retirement and shall be subject to Section 3D.
- F. If the Option is exercised by the executors, administrators, legatees, or distributees of the estate of a deceased optionee, the Company shall be under no obligation to issue stock hereunder unless and until the Company is satisfied that the person(s) exercising the Option is the duly appointed legal representative of the deceased optionee's estate or the proper legatee or distributee thereof.
- G. For purposes of this Section 3, if the last day of the relevant period is a day upon which the Exchange is not open for trading or the Common Stock is not trading on that day, the relevant period will expire at the close of trading on such earlier business day on which the Exchange is open and the Common Stock is trading.

4. Manner of Exercise

- A. Employee or other proper party may exercise the Option only by delivering within the term of the Option written notice to the Company at its principal office in Minneapolis, Minnesota, stating the number of shares as to which the Option is being exercised and, except as provided in Sections 4B(2) and 4C,

accompanied by payment-in-full of the Option price for all shares designated in the notice.

B. The Employee may, at Employee's election, pay the Option price as follows:

- (1) by cash or check (bank check, certified check, or personal check)
- (2) by delivering to the Company for cancellation, shares of Common Stock of the Company which have been held by the Employee for not less than six (6) months with a fair market value equal to the Option price.

For purposes of Section 4B(2), the fair market value of the Company's Common Stock shall be the closing price of the Common Stock on the day immediately preceding the date of exercise on the Exchange. If there is not a quotation available for such day, then the closing price on the next preceding day for which such a quotation exists shall be determinative of fair market value. If the shares are not then traded on an exchange, the fair market value shall be the average of the closing bid and asked prices of the Common Stock as reported by the National Association of Securities Dealers Automated Quotation System. If the Common Stock is not then traded on NASDAQ or on an exchange, then the fair market value shall be determined in such manner as the Company shall deem reasonable.

C. The Employee may, with the consent of the Company, pay the Option price by delivering to the Company a properly executed exercise notice, together with irrevocable instructions to a broker to promptly deliver to the Company from sale or loan proceeds the amount required to pay the exercise price.

5. Payment of Withholding Taxes

Upon exercise of any portion of this Option, Employee shall pay to the Company an amount sufficient to satisfy any federal, state, or local withholding tax requirements which arise as a result of the exercise of the Option or provide the Company with satisfactory indemnification for such payment. Employee may pay such amount by delivering to the Company for cancellation shares of Common Stock of the Company with a fair market value equal to the minimum amount of such withholding tax requirement by (i) electing to have the Company withhold shares otherwise to be delivered with a fair market value equal to the minimum statutory amount of such taxes required to be withheld by the Company, or (ii) electing to surrender to the Company previously owned shares with a fair market value equal to the amount of such minimum tax obligation.

6. Change of Control

A. Notwithstanding Section 2A hereof, the entire Option shall become immediately and fully exercisable upon a "Change of Control" and shall remain fully exercisable until either exercised or expiring by its terms. A "Change of Control" means:

- (1) an acquisition by any individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Securities Exchange Act of 1934, as

amended (the "1934 Act")), (a "Person"), of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) which, together with other acquisitions by such Person, results in the aggregate beneficial ownership by such Person of 30% or more of either

- (a) the then outstanding shares of Common Stock of the Company (the "Outstanding Company Common Stock") or
- (b) the combined voting power of the then outstanding voting securities of the Company entitled to vote generally in the election of directors (the "Outstanding Company Voting Securities");

provided, however, that the following acquisitions will not result in a Change of Control:

- (i) an acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company,
  - (ii) an acquisition by the Employee or any group that includes the Employee, or
  - (iii) an acquisition by any entity pursuant to a transaction that complies with clauses (a), (b) and (c) of Section 6A(3) below; or
- (2) Individuals who, as of the date hereof, constitute the Board of Directors of the Company (the "Incumbent Board") cease for any reason to constitute at least a majority of said Board; provided, however, that any individual becoming a director subsequent to the date hereof whose election, or nomination for election by the Company's shareholders, was approved by a vote of at least a majority of the directors then comprising the Incumbent Board will be considered as though such individual were a member of the Incumbent Board, but excluding, for this purpose, any such individual whose initial membership on the Board occurs as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies by or on behalf of a Person other than the Board; or
- (3) Consummation of a reorganization, merger or consolidation of the Company with or into another entity or a statutory exchange of Outstanding Company Common Stock or Outstanding Company Voting Securities or sale or other disposition of all or substantially all of the assets of the Company ("Business Combination"); excluding, however, such a Business Combination pursuant to which
  - (a) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding Company Common Stock and Outstanding Company Voting Securities immediately prior to such Business Combination beneficially own, directly

or indirectly, a majority of, respectively, the then outstanding shares of common stock and the combined voting power of the then outstanding voting securities entitled to vote generally in the election of directors (or comparable equity interests), as the case may be, of the surviving or acquiring entity resulting from such Business Combination (including, without limitation, an entity that as a result of such transaction beneficially owns 100% of the outstanding shares of common stock and the combined voting power of the then outstanding voting securities (or comparable equity securities) or all or substantially all of the Company's assets either directly or indirectly) in substantially the same proportions (as compared to the other holders of the Company's common stock and voting securities prior to the Business Combination) as their respective ownership, immediately prior to such Business Combination, of the Outstanding Company Common Stock and Outstanding Company Voting Securities,

- (b) no Person (excluding (i) any employee benefit plan (or related trust) sponsored or maintained by the Company or such entity resulting from such Business Combination or any entity controlled by the Company or the entity resulting from such Business Combination, (ii) any entity beneficially owning 100% of the outstanding shares of common stock and the combined voting power of the then outstanding voting securities (or comparable equity securities) or all or substantially all of the Company's assets either directly or indirectly and (iii) the Employee and any group that includes the Employee) beneficially owns, directly or indirectly, 30% or more of the then outstanding shares of common stock (or comparable equity interests) of the entity resulting from such Business Combination or the combined voting power of the then outstanding voting securities (or comparable equity interests) of such entity, and
- (c) immediately after the Business Combination, a majority of the members of the board of directors (or comparable governors) of the entity resulting from such Business Combination were members of the Incumbent Board at the time of the execution of the initial agreement, or of the action of the Board, providing for such Business Combination; or

- (4) approval by the shareholders of the Company of a complete liquidation or dissolution of the Company.

7. Adjustments; Fundamental Change

- A. If there shall be any change in the number or character of the Common Stock of the Company through merger, consolidation, reorganization, recapitalization, dividend in the form of stock (of whatever amount), stock split or other change in the corporate structure of the Company, and all or any portion of the Option shall then be unexercised and not yet expired, appropriate adjustments in the

outstanding Option shall be made by the Company, in order to prevent dilution or enlargement of Employee's Option rights. Such adjustments shall include, where appropriate, changes in the number of shares of Common Stock and the price per share subject to the outstanding Option.

B. In the event of a proposed (i) dissolution or liquidation of the Company, (ii) a sale of substantially all of the assets of the Company, (iii) a merger or consolidation of the Company with or into any other corporation, regardless of whether the Company is the surviving corporation, or (iv) a statutory share exchange involving the capital stock of the Company (each, a "Fundamental Change"), the Management Organization and Compensation Committee (the "Committee") may, but shall not be obligated to:

- (1) with respect to a Fundamental Change that involves a merger, consolidation or statutory share exchange, make appropriate provision for the protection of the Option by the substitution of options and appropriate voting common stock of the corporation surviving any such merger or consolidation or, if appropriate, the "parent corporation" (as defined in Section 424(e) of the Internal Revenue Code of 1986, as amended from time to time, and any regulations promulgated thereunder, or any successor provision) of the Company or such surviving corporation, in lieu of the Option and shares of Common Stock of the Company, or
- (2) with respect to any Fundamental Change, including, without limitation, a merger, consolidation or statutory share exchange, declare, prior to the occurrence of the Fundamental Change, and provide written notice to the holder of the Option of the declaration, that the Option, whether or not then exercisable, shall be canceled at the time of, or immediately prior to the occurrence of, the Fundamental Change in exchange for payment to the holder of the Option, within 20 days after the Fundamental Change, of cash (or, if the Committee so elects in lieu of solely cash, of such form(s) of consideration, including cash and/or property, singly or in such combination as the Committee shall determine, that the holder of the Option would have received as a result of the Fundamental Change if the holder of the Option had exercised the Option immediately prior to the Fundamental Change) equal to, for each share of Common Stock covered by the canceled Option, the amount, if any, by which the Fair Market Value (as defined in this Section 7B) per share of Common Stock exceeds the exercise price per share of Common Stock covered by the Option. At the time of the declaration provided for in the immediately preceding sentence, the Option shall immediately become exercisable in full and the holder of the Option shall have the right, during the period preceding the time of cancellation of the Option, to exercise the Option as to all or any part of the shares of Common Stock covered thereby in whole or in part, as the case may be. In the event of a declaration pursuant to this Section 7B, the Option, to the extent that it shall not have been exercised prior to the Fundamental Change, shall be canceled at the time of, or immediately prior to, the Fundamental Change, as provided in the declaration. Notwithstanding the foregoing, the holder of the Option shall not be entitled to the payment provided for in this Section 7B if

such Option shall have expired or been forfeited. For purposes of this Section 7B only, "Fair Market Value" per share of Common Stock means the fair market value, as determined in good faith by the Committee, of the consideration to be received per share of Common Stock by the shareholders of the Company upon the occurrence of the Fundamental Change, notwithstanding anything to the contrary provided in this Agreement.

8. Miscellaneous

- A. This Option is issued pursuant to the Plan and is subject to its terms. The terms of the Plan are available for inspection during business hours at the principal offices of the Company.
- B. This Agreement shall not create an employment relationship between Employee and the Company and shall not confer on Employee any right with respect to continuance of employment by the Company or any of its affiliates or subsidiaries, nor will it interfere in any way with the right of the Company to terminate such employment at any time.
- C. Neither Employee, the Employee's legal representative, nor the executor(s) or administrator(s) of the Employee's estate, or any person(s) to whom the Option was transferred by will or the applicable laws of distribution and descent shall be, or have any of the rights or privileges of, a shareholder of the Company in respect of any shares of Common Stock receivable upon the exercise of this Option, in whole or in part, unless and until such shares shall have been issued upon exercise of this Option.
- D. This option has been granted to Employee as a purely discretionary benefit and shall not form part of Employee's salary or entitle Employee to receive similar option grants in the future. Benefits received under the Plan shall not be used in calculating severance payments, if any.
- E. The Company shall at all times during the term of the Option reserve and keep available such number of shares as will be sufficient to satisfy the requirements of this Agreement.
- F. The internal law, and not the law of conflicts, of the State of Minnesota, USA, shall govern all questions concerning the validity, construction and effect of this Agreement, the Plan and any rules and regulations relating to the Plan or this Option
- G. Employee hereby consents to the transfer by his/her employer or the Company of information relating to his/her participation in the Plan, including the personal data set forth in this Agreement, between them or to other related parties in the United States or elsewhere, or to any financial institution or other third party engaged by the Company, but solely for the purpose of administering the Plan and this Option. Employee also consents to the storage and processing of such data by such persons for this purpose.

**IN WITNESS WHEREOF**, the parties have caused this Agreement to be executed on the day and year first above written.

GRACO INC.

By \_\_\_\_\_  
«CEO\_Name»  
President and Chief Executive Officer

EMPLOYEE

\_\_\_\_\_  
«F\_Name\_MI» «L\_Name»

**GRACO INC.  
AMENDED AND RESTATED STOCK INCENTIVE PLAN (2006)**

**CHIEF EXECUTIVE OFFICER  
STOCK OPTION AGREEMENT  
(Non-Qualified)**

**THIS AGREEMENT**, made this XXth day of February, 2008, by and between Graco Inc., a Minnesota corporation (the "Company") and <<NAME>> ("<<SNAME>>" or the "Employee").

**WITNESSETH THAT:**

**WHEREAS**, the Company pursuant to the Graco Inc. Amended and Restated Stock Incentive Plan (2006) (the "Plan") wishes to grant this stock option to Employee;

**NOW THEREFORE**, in consideration of the premises and of the mutual covenants contained in this Agreement, the parties agree as follows:

1. Grant of Option

The Company grants to Employee, the right and option (the "Option") to purchase all or any part of an aggregate of «Words» («Number») shares of Common Stock of the Company, par value USD 1.00 per share, at the price of USD «Price» per share on the terms and conditions set forth in this Agreement. The date of grant of the Option is <<DATE>> (the "Date of Grant").

2. Duration and Exercisability

- A. No portion of this Option may be exercised by Employee until the first anniversary of the Date of Grant and then only in accordance with the Vesting Schedule set forth below. In no event shall this Option or any portion of this Option be exercisable following the tenth anniversary of the Date of Grant.

**Vesting Schedule**

<u>Vesting Date</u>	<u>Portion of Option Exercisable</u>
First Anniversary of Date of Grant	25%
Second Anniversary of Date of Grant	50%
Third Anniversary of Date of Grant	75%
Fourth Anniversary of Date of Grant	100%

If Employee does not purchase in any one year the full number of shares of Common Stock of the Company to which he/she is entitled under this Option, he/she may, subject to the terms and conditions of Section 3, purchase such

shares of Common Stock in any subsequent year during the term of this Option. This Option shall expire as of the close of trading at the national securities exchange on which the Common Stock is traded ("Exchange") on the tenth anniversary of the Date of Grant or if the Exchange is closed on the anniversary date or the Common Stock of the Company is not trading on said anniversary date, such earlier business day on which the Common Stock is trading on the Exchange.

- B. During the lifetime of Employee, the Option shall be exercisable only by him/her and shall not be assignable or transferable by him/her otherwise than by will or the laws of descent and distribution.
- C. Under no circumstances may the Option or any portion of the Option granted by this Agreement be exercised after the term of the Option expires.

3. Effect of Termination of Employment

- A. If Employee's employment terminates for any reason other than Employee's gross and willful misconduct, death, retirement (as defined in Section 3D), or disability (as defined in Section 3D), Employee shall have the right to exercise that portion of the Option exercisable upon the date of termination of employment at any time within the period beginning on the day after termination of employment and ending at the close of trading on the Exchange thirty (30) days later.
- B. If Employee's employment terminates by reason of Employee's gross and willful misconduct during employment, including, but not limited to, wrongful appropriation of Company funds, serious violations of Company policy, breach of fiduciary duty or the conviction of a felony, the unexercised portion of the Option shall terminate as of the time of the misconduct. If the Company determines subsequent to the termination of Employee's employment for whatever reason, that Employee engaged in conduct during employment that would constitute gross and willful misconduct justifying termination, the Option shall terminate as of the time of such misconduct. Furthermore, if the Option is exercised in whole or in part and the Company thereafter determines that Employee engaged in gross and willful misconduct during employment which would have justified termination at any time prior to the date of such exercise, the Option shall be deemed to have terminated as of the time of the misconduct and the Company may elect to rescind the Option exercise. Gross and willful misconduct shall not include any action or inaction by <<SNAME>> contrary to the direction of the Board with respect to any initiative, strategy or action of the Company, which action or inaction <<SNAME>> believes is in the best interest of the Company.
- C. If Employee shall die while employed by the Company or an affiliate and shall not have fully exercised the Option, all shares remaining under the Option shall become immediately exercisable. If Employee shall die within thirty (30) days after a termination of employment which meets the criteria of Section 3A above, only those shares vested as of the date of termination shall be exercisable. The executor or administrator of Employee's estate, or any person(s) to whom the Option was transferred by will or the applicable laws of distribution and descent may exercise such exercisable shares at any time during a period beginning on

the day after the date of Employee's death and ending at the close of trading on the Exchange on the anniversary of death one (1) year later.

- D. If Employee's termination of employment is due to retirement or disability, all shares remaining under the Option shall become immediately exercisable. Employee shall be deemed to have retired if the termination of employment occurs for reasons other than the Employee's gross and willful misconduct, death, or disability after Employee (i) has attained age 55 and 10 years of service with the Company or an affiliate, or (ii) has attained age 65. Employee shall be deemed to be disabled if the termination of employment occurs because Employee is unable to work due to an impairment which would qualify as a disability under the Company's long term disability program. Employee may exercise the shares remaining unexercised at any time during a period beginning on the day after the date of Employee's termination of employment and ending at the close of trading on the Exchange on the tenth anniversary of the Date of Grant. If Employee should die during the period between the date of Employee's retirement or disability and the expiration of the Option, the executor(s) or administrator(s) of the Employee's estate, or any person(s) to whom the Option was transferred by will or the applicable laws of distribution and descent may exercise the unexercised portion of the Option at any time during a period beginning the day after the date of Employee's death and ending at the close of trading on the Exchange on the anniversary of death one (1) year later, provided, however, in no event shall the Option be exercisable following the tenth anniversary of the Date of Grant. Notwithstanding anything to the contrary contained in Section 3, if the Employee's employment is terminated by retirement (as defined in this Section 3D) and Employee has not given written notice to the Chair of the Management Organization and Compensation Committee of the Board of Directors (the "Committee"), of Employee's intention to retire not less than six (6) months prior to the date of his retirement, then in such event, for purposes of this Agreement only, said termination of employment shall be deemed to be not a retirement but a termination subject to the provisions of Section 3A, *provided, however*, that in the event that the Committee determines that said termination of employment without six (6) months prior written notice is in the best interests of the Company, such termination shall be deemed to be a retirement and shall be subject to this Section 3D.
- E. If the Option is exercised by the executors, administrators, legatees, or distributees of the estate of a deceased optionee, the Company shall be under no obligation to issue stock hereunder unless and until the Company is satisfied that the person(s) exercising the Option is the duly appointed legal representative of the deceased optionee's estate or the proper legatee or distributee thereof.
- F. For purposes of this Section 3, if the last day of the relevant period is a day upon which the Exchange is not open for trading or the Common Stock is not trading on that day, the relevant period will expire at the close of trading on such earlier business day on which the Exchange is open and the Common Stock is trading.

4. Manner of Exercise

- A. Employee or other proper party may exercise the Option only by delivering within the term of the Option written notice to the Company at its principal office

in Minneapolis, Minnesota, stating the number of shares as to which the Option is being exercised and, except as provided in Sections 4B(2) and 4C, accompanied by payment-in-full of the Option price for all shares designated in the notice.

B. The Employee may, at Employee's election, pay the Option price as follows:

- (1) by cash or check (bank check, certified check, or personal check)
- (2) by delivering to the Company for cancellation, shares of Common Stock of the Company which have been held by the Employee for not less than six (6) months with a fair market value equal to the Option price.

For purposes of Section 4B(2), the fair market value of the Company's Common Stock shall be the closing price of the Common Stock on the day immediately preceding the date of exercise on the Exchange. If there is not a quotation available for such day, then the closing price on the next preceding day for which such a quotation exists shall be determinative of fair market value. If the shares are not then traded on an exchange, the fair market value shall be the average of the closing bid and asked prices of the Common Stock as reported by the National Association of Securities Dealers Automated Quotation System. If the Common Stock is not then traded on NASDAQ or on an exchange, then the fair market value shall be determined in such manner as the Company shall deem reasonable.

C. The Employee may, with the consent of the Company, pay the Option price by delivering to the Company a properly executed exercise notice, together with irrevocable instructions to a broker to promptly deliver to the Company from sale or loan proceeds the amount required to pay the exercise price.

5. Payment of Withholding Taxes

Upon exercise of any portion of this Option, Employee shall pay to the Company an amount sufficient to satisfy any federal, state, or local withholding tax requirements which arise as a result of the exercise of the Option or provide the Company with satisfactory indemnification for such payment. Employee may pay such amount by delivering to the Company for cancellation shares of Common Stock of the Company with a fair market value equal to the minimum amount of such withholding tax requirement by (i) electing to have the Company withhold shares otherwise to be delivered with a fair market value equal to the minimum statutory amount of such taxes required to be withheld by the Company, or (ii) electing to surrender to the Company previously owned shares with a fair market value equal to the amount of such minimum tax obligation.

6. Change of Control

A. Notwithstanding Section 2A hereof, the entire Option shall become immediately and fully exercisable upon a "Change of Control" and shall remain fully exercisable until either exercised or expiring by its terms. A "Change of Control" means:

- (1) an acquisition by any individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Securities Exchange Act of 1934, as amended (the “1934 Act”)), (a “Person”), of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) which, together with other acquisitions by such Person, results in the aggregate beneficial ownership by such Person of 30% or more of either
  - (a) the then outstanding shares of Common Stock of the Company (the “Outstanding Company Common Stock”) or
  - (b) the combined voting power of the then outstanding voting securities of the Company entitled to vote generally in the election of directors (the “Outstanding Company Voting Securities”);

provided, however, that the following acquisitions will not result in a Change of Control:

- (i) an acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company,
  - (ii) an acquisition by the Employee or any group that includes the Employee, or
  - (iii) an acquisition by any entity pursuant to a transaction that complies with clauses (a), (b) and (c) of Section 6A(3) below; or
- (2) Individuals who, as of the date hereof, constitute the Board of Directors of the Company (the “Incumbent Board”) cease for any reason to constitute at least a majority of said Board; provided, however, that any individual becoming a director subsequent to the date hereof whose election, or nomination for election by the Company’s shareholders, was approved by a vote of at least a majority of the directors then comprising the Incumbent Board will be considered as though such individual were a member of the Incumbent Board, but excluding, for this purpose, any such individual whose initial membership on the Board occurs as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies by or on behalf of a Person other than the Board; or
- (3) Consummation of a reorganization, merger or consolidation of the Company with or into another entity or a statutory exchange of Outstanding Company Common Stock or Outstanding Company Voting Securities or sale or other disposition of all or substantially all of the assets of the Company (“Business Combination”); excluding, however, such a Business Combination pursuant to which
  - (a) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding Company Common

Stock and Outstanding Company Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, a majority of, respectively, the then outstanding shares of common stock and the combined voting power of the then outstanding voting securities entitled to vote generally in the election of directors (or comparable equity interests), as the case may be, of the surviving or acquiring entity resulting from such Business Combination (including, without limitation, an entity that as a result of such transaction beneficially owns 100% of the outstanding shares of common stock and the combined voting power of the then outstanding voting securities (or comparable equity securities) or all or substantially all of the Company's assets either directly or indirectly) in substantially the same proportions (as compared to the other holders of the Company's common stock and voting securities prior to the Business Combination) as their respective ownership, immediately prior to such Business Combination, of the Outstanding Company Common Stock and Outstanding Company Voting Securities,

- (b) no Person (excluding (i) any employee benefit plan (or related trust) sponsored or maintained by the Company or such entity resulting from such Business Combination or any entity controlled by the Company or the entity resulting from such Business Combination, (ii) any entity beneficially owning 100% of the outstanding shares of common stock and the combined voting power of the then outstanding voting securities (or comparable equity securities) or all or substantially all of the Company's assets either directly or indirectly and (iii) the Employee and any group that includes the Employee) beneficially owns, directly or indirectly, 30% or more of the then outstanding shares of common stock (or comparable equity interests) of the entity resulting from such Business Combination or the combined voting power of the then outstanding voting securities (or comparable equity interests) of such entity, and
  - (c) immediately after the Business Combination, a majority of the members of the board of directors (or comparable governors) of the entity resulting from such Business Combination were members of the Incumbent Board at the time of the execution of the initial agreement, or of the action of the Board, providing for such Business Combination; or
- (4) approval by the shareholders of the Company of a complete liquidation or dissolution of the Company.

7. Adjustments; Fundamental Change

- A. If there shall be any change in the number or character of the Common Stock of the Company through merger, consolidation, reorganization, recapitalization, dividend in the form of stock (of whatever amount), stock split or other change in

the corporate structure of the Company, and all or any portion of the Option shall then be unexercised and not yet expired, appropriate adjustments in the outstanding Option shall be made by the Company, in order to prevent dilution or enlargement of Employee's Option rights. Such adjustments shall include, where appropriate, changes in the number of shares of Common Stock and the price per share subject to the outstanding Option.

B. In the event of a proposed (i) dissolution or liquidation of the Company, (ii) a sale of substantially all of the assets of the Company, (iii) a merger or consolidation of the Company with or into any other corporation, regardless of whether the Company is the surviving corporation, or (iv) a statutory share exchange involving the capital stock of the Company (each, a "Fundamental Change"), the Management Organization and Compensation Committee (the "Committee") may, but shall not be obligated to:

- (1) with respect to a Fundamental Change that involves a merger, consolidation or statutory share exchange, make appropriate provision for the protection of the Option by the substitution of options and appropriate voting common stock of the corporation surviving any such merger or consolidation or, if appropriate, the "parent corporation" (as defined in Section 424(e) of the Internal Revenue Code of 1986, as amended from time to time, and any regulations promulgated thereunder, or any successor provision) of the Company or such surviving corporation, in lieu of the Option and shares of Common Stock of the Company, or
- (2) with respect to any Fundamental Change, including, without limitation, a merger, consolidation or statutory share exchange, declare, prior to the occurrence of the Fundamental Change, and provide written notice to the holder of the Option of the declaration, that the Option, whether or not then exercisable, shall be canceled at the time of, or immediately prior to the occurrence of, the Fundamental Change in exchange for payment to the holder of the Option, within 20 days after the Fundamental Change, of cash (or, if the Committee so elects in lieu of solely cash, of such form(s) of consideration, including cash and/or property, singly or in such combination as the Committee shall determine, that the holder of the Option would have received as a result of the Fundamental Change if the holder of the Option had exercised the Option immediately prior to the Fundamental Change) equal to, for each share of Common Stock covered by the canceled Option, the amount, if any, by which the Fair Market Value (as defined in this Section 7B) per share of Common Stock exceeds the exercise price per share of Common Stock covered by the Option. At the time of the declaration provided for in the immediately preceding sentence, the Option shall immediately become exercisable in full and the holder of the Option shall have the right, during the period preceding the time of cancellation of the Option, to exercise the Option as to all or any part of the shares of Common Stock covered thereby in whole or in part, as the case may be. In the event of a declaration pursuant to this Section 7B, the Option, to the extent that it shall not have been exercised prior to the Fundamental Change, shall be canceled at the time of, or immediately prior to, the Fundamental Change, as provided in

the declaration. Notwithstanding the foregoing, the holder of the Option shall not be entitled to the payment provided for in this Section 7B if such Option shall have expired or been forfeited. For purposes of this Section 7B only, "Fair Market Value" per share of Common Stock means the fair market value, as determined in good faith by the Committee, of the consideration to be received per share of Common Stock by the shareholders of the Company upon the occurrence of the Fundamental Change, notwithstanding anything to the contrary provided in this Agreement.

8. Miscellaneous

- A. This Option is issued pursuant to the Plan and is subject to its terms. The terms of the Plan are available for inspection during business hours at the principal offices of the Company.
- B. This Agreement shall not confer on Employee any right with respect to continuance of employment by the Company or any of its subsidiaries, nor will it interfere in any way with the right of the Company to terminate such employment at any time.
- C. Neither Employee, the Employee's legal representative, nor the executor(s) or administrator(s) of the Employee's estate, or any person(s) to whom the Option was transferred by will or the applicable laws of distribution and descent shall be, or have any of the rights or privileges of, a shareholder of the Company in respect of any shares of Common Stock receivable upon the exercise of this Option, in whole or in part, unless and until such shares shall have been issued upon exercise of this Option.
- D. The Company shall at all times during the term of the Option reserve and keep available such number of shares as will be sufficient to satisfy the requirements of this Agreement.
- E. The internal law, and not the law of conflicts of the State of Minnesota shall govern all questions concerning the validity, construction and effect of this Agreement, the Plan and any rules and regulations relating to the Plan or this Option.
- F. Employee hereby consents to the transfer to his employer or the Company of information relating to his/her participation in the Plan, including the personal data set forth in this Agreement, between them or to other related parties in the United States or elsewhere, or to any financial institution or other third party engaged by the Company, but solely for the purpose of administering the Plan and this Option. Employee also consents to the storage and processing of such data by such persons for this purpose.

IN WITNESS WHEREOF, the Company, by the Management Organization and Compensation Committee of the Board of Directors, and the Employee have caused this Agreement to be executed and delivered, all as of the day and year first above written.

GRACO INC.  
Management Organization and Compensation  
Committee

By \_\_\_\_\_  
<<CHAIR NAME>>  
Its Chairman

EMPLOYEE

By \_\_\_\_\_  
<<NAME>>

## CERTIFICATION

I, Patrick J. McHale, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Graco Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: \_\_\_\_\_

4-23-08

  
Patrick J. McHale  
President and Chief Executive Officer

**CERTIFICATION**

I, James A. Graner, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Graco Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date:

April 23, 2008

James A. Graner

James A. Graner  
Chief Financial Officer and Treasurer

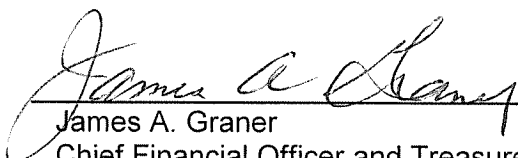
## CERTIFICATION UNDER SECTION 1350

Pursuant to Section 1350 of Title 18 of the United States Code, each of the undersigned certifies that this periodic report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in this periodic report fairly presents, in all material respects, the financial condition and results of operations of Graco Inc.

Date: 4-23-08

  
\_\_\_\_\_  
Patrick J. McHale  
President and Chief Executive Officer

Date: April 23, 2008

  
\_\_\_\_\_  
James A. Graner  
Chief Financial Officer and Treasurer



April 23, 2008

**Electronically Filed**

Securities and Exchange Commission  
Judiciary Plaza  
450 Fifth Street NW  
Washington, DC 20549

Re: Graco Inc.  
First Quarter Report on Form 10-Q  
File No. 001-9249  
CIK No. 0000042888

Gentlemen/Ladies:

Enclosed for filing is the Graco Inc. Quarterly Report on Form 10-Q for the quarter ended March 28, 2008.

Sincerely,

Karen P. Gallivan  
Vice President, General Counsel and Secretary

Enclosure

KPG/nas